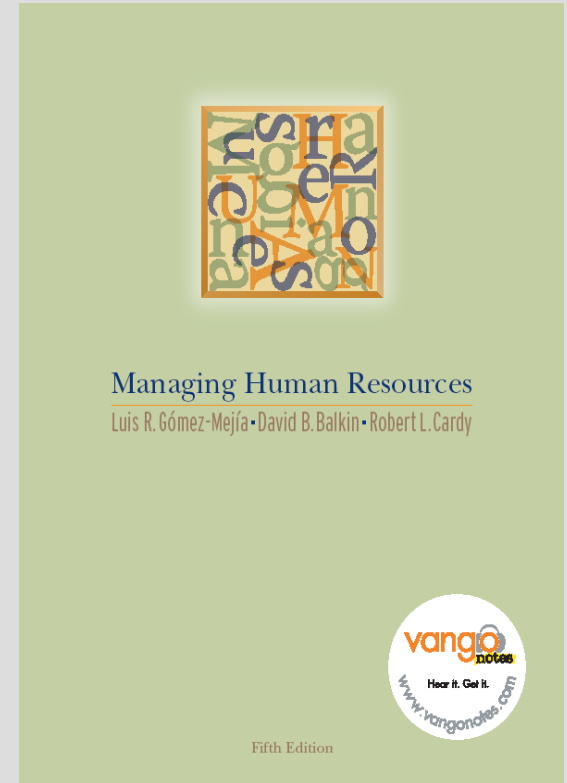


Chapter 10

Managing Compensation



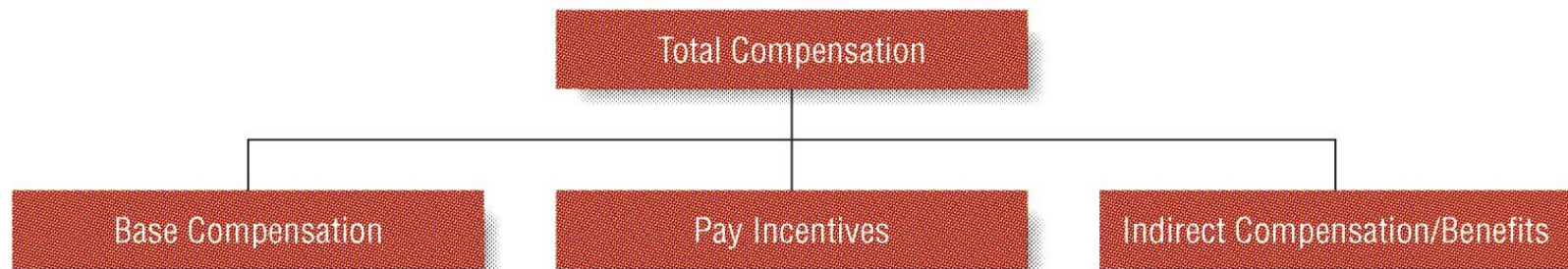
Chapter 10 Overview

- Identify the compensation policies and practices that are most appropriate for a particular firm
- Weigh the strategic advantages and disadvantages of the different compensation options
- Establish a job-based compensation scheme that is internally consistent and linked to the labor market
- Understand the difference between a compensation system in which employees are paid for the skills they use and one in which they are paid for the job they hold
- Make compensation decisions that comply with the legal framework

What Is Compensation?

- Total compensation – The package of quantifiable rewards an employee receives for his or her labors. Includes three components: base compensation, pay incentives, and indirect compensation/benefits

Figure 10.1



Designing a Compensation System

- Internal equity – The perceived fairness of the pay structure within a firm.
- External equity – The perceived fairness in pay relative to what other employers are paying for the same type of labor.



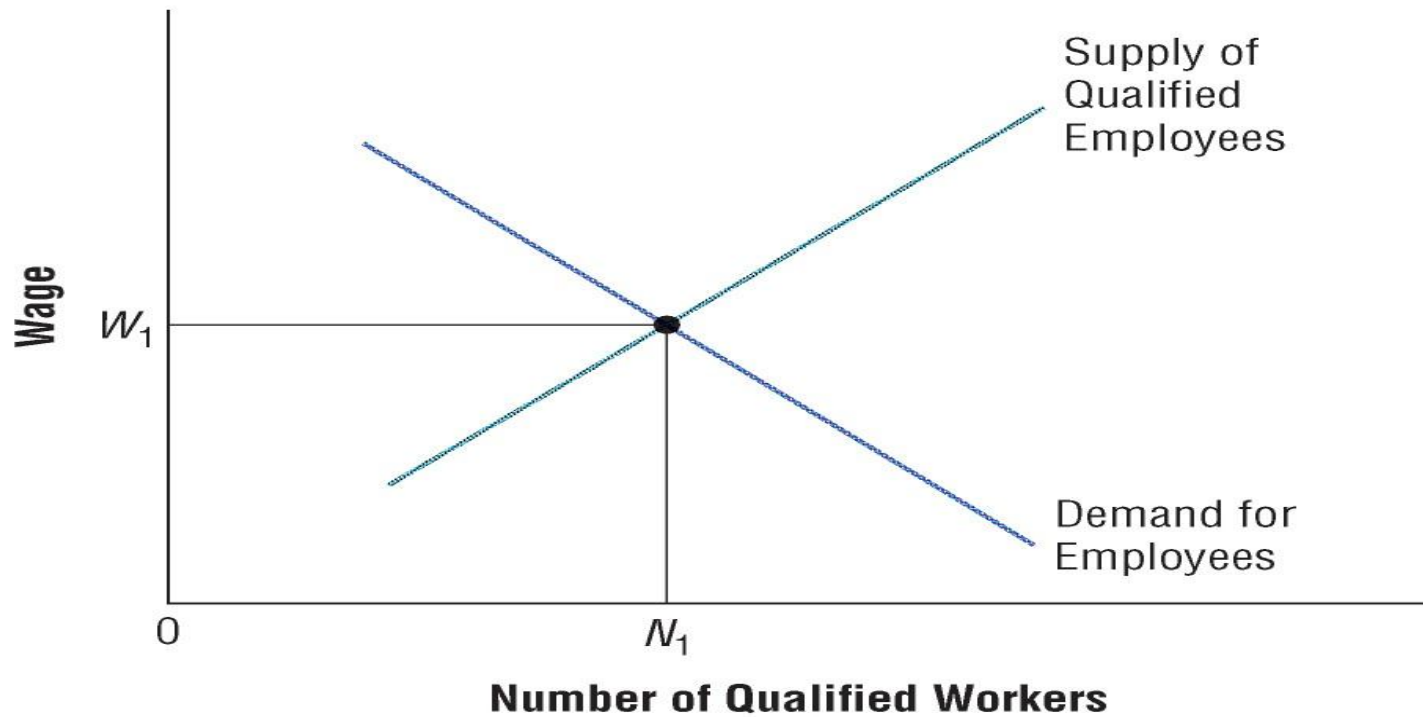
Designing a Compensation System

- The Distributive Justice Model
- Labor Market Model
- Balancing Equity



Labor Market Model

Figure 10.3



Designing a Compensation System



- **Fixed versus Variable Pay**
- **Performance versus Membership**

Job vs. Individual Pay

Job-based pay is best where:

- Technology is stable
- Jobs do not change often
- Employees do not need to cover for one another frequently
- Much training is required to learn a given job
- Turnover is relatively low
- Employees are expected to move up through the ranks over time
- Jobs are fairly standardized within the industry

Job vs. Individual Pay

- Individual-based pay is best where:
- The firm has a relatively educated workforce with both the ability and the willingness to learn different jobs
- The company's technology and organizational structure change frequently
- Employee participation and teamwork are encouraged throughout the organization
- Opportunities for upward mobility are limited
- Opportunities to learn new skills are present
- The costs of employee turnover and absenteeism in terms of lost production are high

Job vs. Individual Pay

- Egalitarian pay system – A pay plan in which most employees are part of the same compensation systems.
- Elitist pay system – A pay plan in which different compensation systems are established for employees or groups at different organizational levels.

Job vs. Individual Pay

- Below-market vs. Above-market compensation
- Monetary vs. Nonmonetary rewards
- Open vs. Secret pay
- Centralization vs. Decentralization of pay decisions
- Summary

Compensation Tools

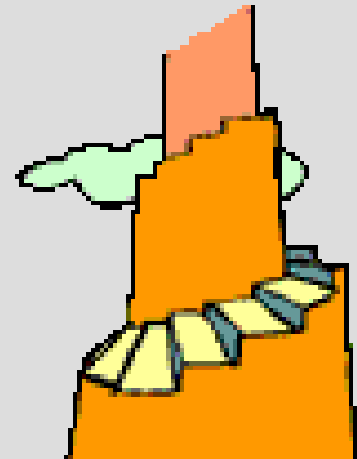
Job-based compensation plans

- Achieving Internal Equity:
Job Evaluation
 - The ultimate goal of job evaluation is to achieve internal equity in the pay structure.



Steps to Achieving Internal Equity

- Step 1: Conduct job analysis
- Step 2: Write job description
- Step 3: Determine job specifications
- Step 4: Rate worth of all jobs using a predetermined system



Steps to Achieving Internal Equity (cont'd)

- Step 5: Create a job hierarchy
- Step 6: Classify jobs by grade levels



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Compensation Tools

Achieving External Equity: Market Surveys

- Step 1: Identify benchmark or key jobs
- Step 2: Establish a pay policy



Compensation Tools

Job-based compensation plans

Achieving Individual Equity: Within-Pay-Range Positioning Criteria

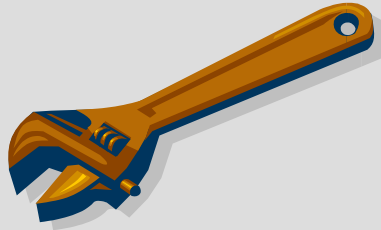
- Individual equity – *The perceived fairness of individual pay decisions.*

Market Salary Data for Selected Benchmark Office Jobs

Figure 10.14

Benchmark Jobs	Weekly Pay Percentile			Weekly Pay Average
	25th	50th	75th	
1. Customer Service Representative	\$400	\$500	\$650	\$495
2. Credit and Collection Clerk	\$400	\$450	\$550	\$455
3. Accounting Clerk	\$370	\$425	\$475	\$423
4. Word Processing Operator	\$380	\$390	\$430	\$394
5. Clerk-Typist	\$330	\$350	\$400	\$343

Compensation Tools



- Evaluating job-based compensation plans
- Suggestions for practice
- Skill-based compensation plans

The Legal Environment and Pay Systems Governance

- The Fair Labor Standards Act
 - Exempt/Non-exempt employees
 - Minimum wages
 - Overtime
- The Equal Pay Act
 - Comparable worth
 - Role of the Office of Federal Contract Compliance

Summary and Conclusions

- What is compensation?
- Designing a compensation system
- Compensation tools
- The legal environment & pay systems governance